FILE COPY

[illegible]

No. [illegible] 13

[illegible]

Appellant,

vs.

[illegible] and [illegible], State [illegible] of the State of Wisconsin.

[illegible]

STATEMENT AS TO JURISDICTION.

John M. [illegible],
Counsel for Appellant.

INDEX.

Subject Index.

Table of Cases Cited.

Statutes Cited.

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1937

No. 888

EARLE S. WELCH,

Appellant,

vs.

ROBERT K. HENRY AND SOLOMON LEVITAN, STATE TREASURER OF THE STATE OF WISCONSIN,

Appellee.

STATEMENT OF THE BASIS OF THE JURISDICTION OF THE SUPREME COURT OF THE UNITED STATES TO REVIEW THE JUDGMENT OF THE SUPREME COURT OF THE STATE OF WISCONSIN IN THE ABOVE CAUSE.

This statement is presented in compliance with Rule 12 of the Revised Rules of the Supreme Court of the United States for the purpose of disclosing the basis upon which it is contended that the Supreme Court has jurisdiction upon appeal to review the judgment of the Supreme Court of the State of Wisconsin in the above entitled cause.

It is believed that the jurisdiction of the Supreme Court of the United States is sustained by Paragraph A of Section 237 of the Judicial Code (Section 344 of Title 28 of the United States Code) for the reason that the appeal is

sought from a judgment in the highest court of a State in which a decision could be had in a case in which there is drawn in question the validity of a statute of the State of Wisconsin on the ground of its being repugnant to the Constitution of the United States and the decision is in favor of its validity.

The statute of the State of Wisconsin, the validity of which is involved, is Section 6 of Chapter 15 of the Laws of Wisconsin for 1935, published March 27, 1935. That section is entitled "Emergency Relief Tax on Certain 1933 Dividends." The material portions thereof are as follows:

"(1) For the purpose of this section.

"(a) 'Person' shall mean persons other than corporations as defined in subsection (1) of section 71.02.

"(b) 'Dividends' shall mean all dividends derived from stocks whether paid to shareholders in cash or property received in the calendar year 1933, or corresponding fiscal year, and deductible under subsection (4) of section 71.04.

"(d) 'Net dividend income' shall mean gross dividend income less seven hundred and fifty dollars.

"(2) To provide revenues for relief purposes there is levied and there shall be assessed, collected, and paid, an emergency tax upon the net dividend income of all persons in the calendar year 1933 or corresponding fiscal year at the following rates:

"(a) On the first two thousand dollars of net dividend income or any part thereof, at the rate of one per cent.

"(b) On the next three thousand dollars of net dividend income or any part thereof, at the rate of three per cent.

"(c) On all net dividend income above five thousand dollars, at the rate of seven per cent."

The judgment of the Supreme Court of the State of Wisconsin here sought to be reviewed was rendered on the 15th

day of January, 1938. The application for appeal is presented this 17th day of February, 1938.

The plaintiff and appellant was assessed a tax under the purported authority of Section 6 of Chapter 15 of the Laws of 1935 in the sum of five hundred forty-five and 71/100 dollars ($545.71) which he paid under protest. He then instituted this action in the Circuit Court for Eau Claire County for the purpose of securing the repayment of the money thus paid. In adopting this procedure he followed the remedy specifically provided by Paragraph 5 of Subsection 5 of said Statute. The complaint sought the repayment of the tax paid on the ground that Section 6 of Chapter 15 of the Laws of 1935 was in violation of the Constitution of the State of Wisconsin and in violation of Section 1 of the Fourteenth Amendment to the Constitution of the United States. No other grounds for the cause of action were alleged except the violation of the State and Federal Constitutions by the Act in question. It is believed, therefore, that the question of the validity of the Statute under the Constitution of the United States was raised in the first instance in the complaint and that the questions raised are substantial because of the fact that the plaintiff and appellant had been assessed a tax under the purported authority of the statute which he had paid under protest and the repayment of which was sought.

The defendant and appellee filed a demurrer to the original complaint on the ground that it did not state facts sufficient to constitute a cause of action. The Circuit Court for Eau Claire County entered an order overruling this demurrer on the ground that the Act in question did violate Section 1 of the Fourteenth Amendment to the Constitution of the United States as appears from the decision of that court which constitutes a part of the record herein and a copy of which is hereto attached. The defendant and present appellee appealed from the order overruling the

demurrer to the Supreme Court of the State of Wisconsin which reversed the action of the Circuit Court for Eau Claire County and remanded the cause with directions to sustain the demurrer. In so doing the Supreme Court of Wisconsin recognized that the plaintiff and appellant had questioned the validity of the Statute under the Fourteenth Amendment to the Constitution of the United States and passed upon that contention adversely as indicated by the opinion filed in that appeal and by the dissenting opinion of a minority of the court, a copy of which is hereto attached. Thereafter the case was remanded to the Circuit Court for Eau Claire County which entered an order sustaining the demurrer pursuant to the mandate of the Supreme Court of the State of Wisconsin and granted the plaintiff and appellant leave to file an amended complaint. Such an amended complaint was filed in which again the invalidity of the Statute in question under the provisions of the Constitution of the United States was alleged. A demurrer was filed to the amended complaint of the plaintiff which was sustained and the defendant not choosing to plead further a judgment was entered from which an appeal was again taken to the Supreme Court of the State of Wisconsin. The judgment of that court, from which the present appeal to the Supreme Court of the United States is sought, affirmed the judgment of the Circuit Court for Eau Claire County dismissing the complaint and in the opinion filed therewith, a copy of which is hereto attached, the contentions of the plaintiff and appellant as to the invalidity of the Statute under the Federal Constitution were again recognized, considered and decided adversely to him and in favor of the validity of the Statute.

No great list of authorities seems necessary to establish the proposition that a State taxing statute must conform

to the requirements of the Fourteenth Amendment to the Federal Constitution.

Louisville Gas and Electric Co. v. *Coleman*, 277 U. S. 32.

The many cases in which appeals and writs of error have been granted to review the decisions of State courts as to the validity of taxing statutes under the Federal Constitution all support the jurisdiction in this case. These include

Schlesinger v. *Wisconsin*, 270 U. S. 230;
Colgate v. *Harvey*, 296 U. S. 404;
Senior v. *Braden*, 295 U. S. 422,
Fisher's Blend Station v. *Commission*, 297 U. S. 650;

and many others.

Respectfully submitted,

JOHN M. CAMPBELL,
Attorney for Appellant.

EXHIBIT "A".

CIRCUIT COURT, EAU CLAIRE COUNTY.

EARLE S. WELCH, *Plaintiff*,

vs.

ROBERT K. HENRY, State Treasurer of the State of Wisconsin, *Defendant*.

Decision of Court.

The plaintiff brought suit against the defendant to recover $545.71, with interest from May 15, 1935, which was paid under protest by the plaintiff to the defendant as an emergency tax levied against the plaintiff under the provisions of Section 6, of chapter 15 of the laws of 1935. The defendant demurred to the complaint on the ground that it appears on the face thereof that it does not state facts sufficient to constitute a cause of action.

By this Chapter, which was published March 27, 1935, the Legislature levied and directed to be collected five different emergency taxes:

(1) An emergency tax on individuals generally based on their net incomes of 1934;

(2) An emergency inheritance tax based on transfers thereafter made;

(3) An emergency tax on the business of telephone companies transacted during the year 1934;

(4) An emergency tax on the business of electric light and power companies transacted during the year 1934; and

(5) An emergency tax levied on persons who received dividends from corporate profits during the year 1933.

The tax in question is a tax of the fifth class. It was levied and collected pursuant to the provisions of section 6, of this chapter. The statute provides that the only remedy of a taxpayer who desires to contest the validity of the tax is to

pay the tax under protest and bring suit against the State Treasurer to recover it back.

The complaint alleges that in the year 1933, the plaintiff's total gross income was $13,383.26, of which amount $12,156.10 was money received by him as dividends from certain corporations. It alleges that his total losses and expenses for that year were $11,061.97, leaving an actual net income, including dividends, of only $2,321.29, and that under the laws of 1933, pursuant to which he made his return in 1934, his total losses and deductions, including dividends, were $23,195.57.

The plaintiff was assessed under this statute on his 1933 income for having received a gross dividend income of $12,156.10 and for having received a net dividend income of $750.00 less than the gross amount. This was in accordance with the provisions of the statute.

The sole question involved in this case is the constitutionality of section 6, of chapter 15, of the laws of 1935.

It is argued by plaintiff's counsel that the statute is unconstitutional on three grounds:

(1) That the statute is unconstitutional because the tax is not based on an income, gain or profit, but is based on one item of gross income without deducting losses or expenses of any kind and without allowing any deduction, except an arbitrary one of $750.00.

(2) That the statute is unconstitutional because it arbitrarily takes private property for public use in violation of vested rights. It is admitted that a statute may be lawfully made retroactive during the period when the annual tax is being collected and disbursed. It is admitted that a statute may also be made retroactive when necessary to collect a tax which a taxpayer legally or equitably owes, and for the purpose of supplying a remedy where existing law is inadequate to give complete relief. It is contended that when a taxpayer has fully paid his tax according to law, when no tax legal or equitable exists and when the annual period for its collection and disbursement has expired that the legislature is without power by a retroactive statute to create an obligation to pay a tax on past transactions where no obligation previously existed.

In the following cases statutes somewhat similar in nature were held to be invalid:

Forbes Pioneer Boat Line v. *Board of Commissioners*, 258 U. S. 238, 66 L. Ed. 647;

Nichols v. *Coolidge*, 247 U. S. 531, 71 L. Ed. 1184;

Norris v. *Tax Commission*, 205 Wisconsin, 626.

(3) It is claimed that the statute is unconstitutional because it denies to the plaintiff and to other persons who received dividends during the year 1933, equal protection of the laws.

It is argued by counsel for the defendant that no statute should be held to be unconstitutional if its validity can be sustained by any reasonable construction or if there is a reasonable doubt as to its validity. It is also argued that in the classification of persons and property for taxation it is proper for the Legislature to make different provisions applicable to different classes where reasonable and necessary to do so in order to provide a fair and equitable distribution of the burden of taxation and that such a classification is valid although it does not always work out equitably in the distribution of this burden to a mathematical accuracy.

There is no doubt as to the correctness of these contentions of defendant's counsel. They have been stated so often by courts, State and Federal, that they have become too familiar to require the citation of authorities for their support. It must also be remembered that none of these rules mean that the constitution, State or Federal, is no longer in force. All persons within their jurisdiction are entitled to constitutional protection. The duty to support the constitution does not end with the taking of an official oath.

I find it unnecessary to determine the two first objections raised to the validity of this statute as I am basing my decision on the ground that the statute in question denies to the plaintiff equal protection of the laws.

The emergency tax levied by section 6 discriminates against one class of taxpayers. The tax is levied on stockholders of corporations who received from corporate profits dividends in the year 1933. All other taxpayers are exempt from the tax. Under most income tax laws heretofore en-

acted where a corporation pays a tax on its profits it has been regarded as unfair to levy another tax on the same profit against the individual stockholders. In this instance, however, the order of things is reversed with a vengence and the individual stockholder is singled out as the only person against whom the tax is levied. No other emergency tax, either by section 6 or by any other section of the chapter, is levied against any person on account of the receipt by him of any other kind of income in the year 1933. No other tax is levied tending to equalize this inequality. In the emergency tax levied by section 2 of this chapter on the 1934 incomes, stockholders who have been subjected to this special dividend tax are again included and assessed like all other taxpayers and are subjected to another and additional emergency tax.

In the equitable distribution of taxation persons receiving dividends in the year 1933 should not be classified less favorably than persons receiving other kinds of income that year. For the purpose of taxation the income was not materially different than the following kinds: Salaries paid officers of private corporations; salaries paid to public officials; interest; rents; profit and income of all kinds received by individuals and corporations generally, unless some good reason appeared for some legislative exception.

The statute is also discriminatory against the class of persons receiving dividends in the year 1933 when compared with other classes of persons when such other classes are assessed at all. It discriminates in being more drastic in limiting deductions for losses, expenses and exemptions. It is more drastic in the rapid increase of the graduated rate. For some reason one class only was selected to bear the entire burden of the emergency tax in question. This class was subjected to an unusually inequitable burden.

The Legislature may lawfully exempt from taxation certain classes of property or certain classes of income or apply different rules to different classes of taxpayers where some substantial difference exists in the various classes and some reasonable ground exists justifying the classification. Such statutes have been frequently sustained. If the inequality is not substantial and only results from the application of some necessary general rule of law, the validity of the stat-

ute will be sustained. If the inequality in one respect is offset or equalized by some other provision of the statute, the validity of the statute will be sustained. The Legislature has a broad discretion on this subject in distributing the burden of taxation in a just and equitable manner so long as it does not resort to an arbitrary classification. If no real and substantial difference exists in the different classes as appears from the purpose for which the statute was enacted and if an arbitrary and inequitable distribution of the burden of taxation has been made violating plain principles of justice, then the statute should be condemned as denying to one class equal protection of the laws.

In this case the classification is purely arbitrary. It has no logical bearing on the purpose for which the statute was enacted, or on the moral duty or ability of the class discriminated against to pay the burden of taxation. A tax distributed among various classes of taxpayers but imposing 100% of the tax on one relatively small class and nothing on any of the other classes is about as arbitrary, inequitable and unjust as could well be imagined. It is useless to argue that there was an attempt in the classification to make a fair and equitable distribution of the burden of this tax when in fact no distribution of any kind among the different classes was made or attempted.

This case is not one which makes it necessary to analyze and discuss in detail the great mass of authorities which might be cited on this subject. In the following cases statutes were held to be unconstitutional which were much less objectionable than the statute involved in this case:

Travis v. *Yale & Town Mfg. Co.*, 252 U. S. 60, 64 L. Ed. 460;

F. S. Royster Guano Co. v. *Virginia*, 253 U. S. 412, 64 L. Ed. 989;

Air-Ways El. A. Co. v. *Day*, 266 U. S. 71, 69 L. Ed. 169;

Louisville Gas & El. Co. v. *Coleman*, 277 U. S. 32, 72 L. Ed. 770;

Nat. L. Ins. Co. v. *United States*, 277 U. S. 508, 72 L. Ed. 968;

Colgate v. *Harvey* (U. S.), 80 L. Ed. 225;

Ed Schuster, Inc. v. *Henry*, 261 N. W. (Wis.) 20.

In *Colgate* v. *Harvey*, 80 L. Ed. 225, one of the latest decisions of the United States Supreme Court on this subject, it was held that a statute was invalid which levied an income tax on one class of persons for interest collected on money loaned without the state and exempted another class for interest collected on money loaned within the state. The court held that the distinction in the classification was an arbitrary one considering the purpose for which the statute was enacted and that the statute denied to one class equal protection of the laws. That decision serves to illustrate how far beyond the borderline of validity the Legislature went in enacting the statute in question. The demurrer to the complaint will be overruled.

JAMES WICKHAM,
Circuit Judge.

EXHIBIT "B".

IN SUPREME COURT, STATE OF WISCONSIN,

AUGUST CALENDAR, 1936. JANUARY TERM, 1937.

No. 23

EARLE S. WELCH, *Respondent*,

vs.

ROBERT K. HENRY, State Treasurer, *Appellant*.

Appeal from an Order of the Circuit Court for Eau Claire County. James Wickham, Circuit Judge. *Reversed*.

This was an action commenced on July 23, 1935, by Earle Welch, as plaintiff, against Robert K. Henry, State Treasurer of the state of Wisconsin, defendant, to recover the sum of $545.71 paid by plaintiff under protest as an income tax pursuant to sec. 6, Ch. 15, Laws of 1935. The complaint alleged that during the year 1933, plaintiff received a total income of $13,383.26, of which $12,133.60 was in the form of dividends from Wisconsin corporations; that under the income tax laws then in effect, Ch. 71, Stats. 1933, plaintiff was entitled to deduct from his gross income the full

amount of such dividends; that in addition plaintiff was entitled to deductions from his gross income for 1933 amounting to $11,161.97, plus donations of $100, making a total of $11,161.97; that as a result thereof the plaintiff had no net income for the year 1933 subject to tax; that shortly prior to the 15th day of May, 1935, defendant received from the Wisconsin Tax Commission a bill for emergency relief tax assessed under the provisions of sec. 6, Ch. 15, Laws of 1935, in the sum of $556.84, which amount less a 2% discount plaintiff paid under protest; that sec. 6, Ch. 15, Laws of 1935, is unconstitutional and invalid. Judgment is demanded against the defendant as State Treasurer of the state of Wisconsin in the sum of $545.71, together with interest. Defendant demurred to the complaint upon the ground that the same does not state facts sufficient to constitute a cause of action against him. On February 7, 1936, the lower court entered an order overruling defendant's demurrer. Defendant appeals.

WICKHEM, *J.*

The sole question upon this appeal is the constitutionality of sec. 6, Ch. 15, Laws of 1935, which is entitled, "Emergency Relief Tax on Certain 1933 Dividends."

The material portions of the statute here in question are as follows:

"(1) For the purpose of this section

"(a) 'Person' shall mean persons other than corporations as defined in subsection (1) of section 71.02.

"(b) 'Dividends' shall mean all dividends derived from stocks whether paid to shareholders in cash or property received in the calendar year 1933, or corresponding fiscal year, and deductible under subsection (4) of section 71.04.

"(d) 'Net dividend income' shall mean gross dividend income less seven hundred and fifty dollars.

"(2) To provide revenues for relief purposes there is levied and there shall be assessed, collected, and paid, an emergency tax upon the net dividend income of all

persons in the calendar year 1933 or corresponding fiscal year at the following rates:

"(a) On the first two thousand dollars of net dividend income or any part thereof, at the rate of one per cent.

"(b) On the next three thousand dollars of net dividend income or any part thereof, at the rate of three per cent.

"(c) On all net dividend income above five thousand dollars, at the rate of seven per cent."

Plaintiff's first contention is that the act is discriminatory and obnoxious to the provisions of the 14th amendment to the United States Constitution as well as to secs. (1) and (22) of Art. 1, Wisconsin constitution. These sections read as follows:

"SECTION 1. All men are born equally free and independent, and have certain inherent rights; among these are life, liberty and the pursuit of happiness; to secure these rights, governments are instituted among men, deriving their just powers from the consent of the governed."

"SECTION 22. The blessings of a free government can only be maintained by a firm adherence to justice, moderation, temperance, frugality and virtue, and by frequent recurrence to fundamental principles."

Both plaintiff and defendant concede that while the legislature may classify persons for purposes of taxation, the classification must be based on reasonable differences or distinctions which distinguish the members of a class from those of another in respects germane to some general and public purpose or object of the particular legislation. *Louisville Gas & Electric Co.* v. *Coleman*, 277 U. S. 32. This rule is well settled and calls for no further exposition here. Plaintiff's claim is based upon the fact that under the law as it existed in 1933, and upon which plaintiff reported and paid his income taxes for that year, there was allowed to him as a deduction dividends received from Wisconsin corpora-

tions. The emergency relief tax enacted in 1935 levied a graduated tax upon dividends from Wisconsin corporations received in 1933 and at that time deductible from plaintiff's gross income. It is contended that there is no difference between plaintiff and persons receiving no income from dividends paid by Wisconsin corporations that reasonably warrants such a classification. It is not contended that the legislature in 1933 could not have abolished the exemption of this dividend income if the net result had merely been to throw into the total of assessable income for the year 1933, the Wisconsin dividend of a particular taxpayer and subject it to the normal taxes for that year. However, had the legislature done this, the result would have been a general income tax, and the dividend income would have been treated on a parity with all of the taxpayer's other income. It would have been subject to the same deductions, and he could have subtracted from it the same losses that he could as against any other sort of income and it would have been taxed on an absolute parity with such other incomes. It is obvious that the question here is quite different. The question is whether the legislature having theretofore exempted dividends received from Wisconsin corporations from a normal tax may by separate act subject them to a special tax for emergency relief purposes. It is clear to us that there is but a single ground of differentiation, and that the classification must stand or fall upon this ground. Does the fact that the taxpayers who received dividends of Wisconsin corporations were exempt from a normal tax in 1933 so differentiate them from other persons receiving dividends during this year as to justify the subsequent levy upon them of a special income tax to meet a particular public emergency? As thus stated, two questions are involved: (1) Is the classification a valid one, and (2) whatever the answer to this may be, is there in fact any discrimination against a person receiving income from Wisconsin dividends. If the first question receives an affirmative answer, the law is valid so far as its alleged discriminatory features are concerned. If the second question receives a negative answer, plaintiff has no standing to attack it since his rights are not adversely affected. It is our conclusion that the fact

that the income had previously been exempt from a normal tax is a sufficient reason for giving it different treatment upon the emergency tax. It does not impress us as material upon the issue of discrimination whether the previous exemption was accomplished by taxing all income except that derived from dividends of Wisconsin corporations or by taxing all income and allowing the deduction of income from this source. These are mere matters of form. The net result was that this income had not been subjected to a normal tax. In searching for subjects of emergency taxation, the legislature for this very reason might impose a special tax for emergency relief upon the recipients of this type of income. The reason for imposing a special burden is as valid as that for exempting it from the normal burden. See, *State ex rel. Atwood* v. *Johnson*, 170 Wis. 218, 175 N. W. 589; *C. & N. W. R. Co.* v. *State*, 128 Wis. 553, 108 N. W. 557. Some point is made of the fact that the emergency tax upon this particular type of income is at a rate higher than the normal tax. We are not satisfied that such is the case. While the rates are nominally higher, it may well have been considered that this income, if added to the balance of the taxpayer's income, would normally be taxed in the higher rather than the lower brackets of the normal tax, and this factor could be taken account of in establishing rates for the special tax. Recognition of this principle appears to have been given in the case of *Colgate* v. *Harvey*, 296 U. S. 404. Whatever may be the proper conclusion as to the classification, we do not think plaintiff can claim to have been discriminated against, when the whole pattern of tax legislation is considered. It is not apparent to us that one who is exempt from the burden of annually responding to a normal income tax has been injured by requiring him to meet that of an occasional emergency tax. It might with equal or greater force be argued that the original act discriminated against persons receiving income from sources other than dividends of Wisconsin corporations. This being true, plaintiff has no standing to object to the classification adopted.

It is also contended that there is discrimination as between members of the same class for the reason that only

a fixed sum is deductible from the net income which does not vary in accordance with the circumstances or amount of the net income of a stockholder receiving dividend income from Wisconsin corporations. We do not consider this objection to be valid. Considering the class to consist of all persons receiving dividends from Wisconsin corporations, all are treated alike, taxed alike, given the same deduction, and the same rate of tax. So long as this is properly treated as an income tax, the progressive character of the rates cannot be considered to be objectionable. It is our conclusion that there is no clear indication here that the purpose or effect of the act is a hostile or oppressive discrimination against particular persons or classes. *Beers* v. *Glynn*, 211 U. S. 477, *Citizens Telephone Co.* v. *Fuller*, 229 U. S. 322.

The foregoing consideration of plaintiff's claim that the act is discriminatory took no account of the retroactive features of the law under examination. It now becomes proper to consider plaintiff's objection that the law is invalid because of these features. It is plaintiff's claim that the legislature is authorized to make income tax provisions retroactive during the year of enactment and during the preceding year where the tax upon such preceding year has not been determined and paid, but that it is beyond the power of the legislature to tax dividends received in 1933 by a statute passed in 1935. We deem this objection to be unsound. It was held in *Van Dyke* v. *Tax. Comm.*, 217 Wis. 528, 259 N. W. 700, that an income tax which is given retroactive effect by the legislature cannot properly be assailed on constitutional grounds if it applies to the year in which the law is enacted *or if it applies to prior but recent transactions*. This is also the rule as announced by the United States Supreme Court. *Brushaber* v. *Union Pacific R. Co.*, 240 U. S. 1; *Lynch* v. *Hornby*, 247 U. S. 339; *Cooper* v. *U. S.*, 280 U. S. 409. In the Cooper case it is said that,

> "That the questioned provision cannot be declared in conflict with the Federal Constitution merely because it requires gains from prior but recent transactions to be treated as part of the taxpayer's gross in-

come has not been open to serious doubt since. *Brushaber* v. *Union Pacific R. Co.*, 240 U. S. 1, and *Lynch* v. *Hornby*, 247 U. S. 339."

It is our conclusion (1) that under this rule the legislature may measure an income tax by the income of a year sufficiently recent so that the income of that year may reasonably be supposed to have some bearing upon the present ability of the taxpayer to pay the tax, and (2) that the legislature, subject to this limitation, may go back at least to the most recent year for which they have returns furnishing data upon which to estimate the total return of the tax to the state. While the present tax may approach or reach the limit of permissible retroactivity, it does not exceed it.

The next two contentions of plaintiff may properly be considered together. They are that the tax is not authorized by the authority contained in section 1, Art. VIII, Wisconsin constitution for the imposition of taxes on income because while it purports to be a tax upon income it is either (a) a graduated tax on gross receipts in which case it is void under the authority of *Schuster* v. *Henry*, 218 Wis. 506, 261 N. W. 20, and *Stewart Dry Goods Co.* v. *Lewis*, 294 U. S. 550, or (b) that, being levied solely upon income from a particular kind of property, the subject of the tax is so closely bound up with the ordinary attributes of ownership that it amounts to a tax upon the property itself and as such violates the constitutional requirement of uniformity. Article VIII, section 1, provides as follows:

> "the rule of taxation shall be uniform, and taxes shall be levied upon such property with such classifications as to forests and minerals, including or separate or severed from the land, as the legislature shall prescribe. Taxes may also be imposed on incomes, privileges and occupations, which taxes may be graduated and progressive, and reasonable exemptions may be provided."

The general principle underlying these contentions is that a tax measured in terms of income from a business, occupation or a particular kind of property is not an in-

come tax within the meaning of that term as used in the constitution, but that it constitutes either an occupation or privilege tax in which case it must not be levied retrospectively, or a property tax, in which case it must satisfy the constitutional requirements of uniformity. The contention proves too much. If there is any validity to the contention, then a tax may only be considered an income tax if levied upon all the actual net income of a taxpayer. The exclusion from the operation of a taxing statute of the income from any particular source would destroy the income character of the tax. This would follow whether the statute expressly subjected all income to its operation, and then allowed as a deduction income from particular kinds of property, or was made applicable to less than all of the taxpayer's income. As stated before, these are mere matters of form. Hence, if plaintiff's contention be true, the income tax law of 1933 was no more an income tax than is the special act under examination here. It is our conclusion that a tax upon the net income from a particular kind of property is within the constitutional description of income taxes and is not a privilege tax or one upon the property from which the income is derived. This is, of course, true only if the tax be upon the net income. A tax upon the gross income of particular kinds of property or particular taxpayers or a particular business is doubtless within the condemnation of the *Stewart* and the *Schuster* cases, *supra*, and constitutes in effect a tax upon the property itself. However, taxation upon income from dividends falls in a different class. In cases to which this tax is applicable, the income is in a real sense net income to the taxpayer. The expenses of producing the income have been allowed to the corporation prior to its distribution as a dividend. There are no losses or expenses to be deducted so far as this income is concerned, and if there were, the gross deduction of $750 may well be supposed sufficiently to meet any minor expenses that may conceivably be imagined in connection with the production of the income. Thus, the tax is not upon gross receipts, or at least the gross receipts are net receipts so far as the particular items of income is concerned. It is our conclusion, therefore, that the tax in ques-

tion constitutes an income tax; that a reasonable deduction is allowed to the taxpayer; and that being an income tax, there is no constitutional objection to the imposition of a graduated or progressive rate of tax upon such income. These conclusions sufficiently deal with the contention that the tax is a privilege tax and that it cannot be retroactively applied. It follows that the order must be reversed.

By the court: Order reversed, and cause remanded with directions to sustain the demurrer.

EXHIBIT "C".

IN SUPREME COURT, STATE OF WISCONSIN.

August Calendar, 1936. January Term, 1937.

No. 23.

EARLE S. WELCH, *Respondent*,

v.

ROBERT K. HENRY, State Treasurer, *Appellant*.

FOWLER, *J.* (dissenting):

This is an action to recover a tax paid under protest assessed under sec. 6, Ch. 15, Laws of 1935, enacted March 27, 1935, which by its terms imposes an emergency tax on persons who received dividends from Wisconsin corporations during the year 1933 which were then deductible from the income on which the normal income tax of the person who received them was computed.

The claimed basis for the imposition of the tax upon the species of income covered by it and not imposing it upon any other species of income during that year, is that all other species of income were included in the income on which the normal income tax was computed, and were thus taxed, while the dividends covered by the section were not included and not taxed. It is reasoned that as these

dividends might properly have been taxed during the year 1933 and were not then taxed, it is proper to tax them now, by analogy to the rule that property or income omitted from taxation during one year may be taxed in subsequent years on discovery of the omission.

That reasoning would support a tax imposed by a statute of 1935 on church property and all other property exempt from taxation by the laws as they stood in 1933. Would such a tax be legal, or would it be an illegal interference with vested property rights? This question was propounded in *First National Bank* v. *Covington*, 103 Fed. 523, 527, where it is said that the court would not say that there might not be an extreme case where retroactive taxation for a previous year upon property then not subject to taxation at all might be levied, but points out that if the power exists at all, there is no limit to its exercise, and under it property exempt by law might be taxed for so many years back that it would be wholly confiscated. The latter of course would not be permissible.

In the *Covington* case *supra*, a state statute by its terms provided that by reason of the fact that a prior statute taxing the franchises of national banks had been declared invalid by the Supreme Court of the United States, a tax was imposed on the shares of stock of such banks within the state, and by a section of the latter statute it was applied retroactively to include taxation of shares during the period between the two enactments. The retroactive section was held unconstitutional and a preliminary injunction was granted against assessing any tax under the latter statute for the period prior to its enactment. The period reached back several years, but the injunction went against taxation for the last year of the period as well as the first. It is stated in 2 Cooley on Taxation, (4th Ed.) sec. 520, upon the authority of this case, that "It would seem that a statute cannot impose retroactive taxation for previous years upon a class of property not then subject to taxation," and this statement is cited with approval in *Norris* v. *Tax Commission*, 205 Wis. 626, 628, 237 N. W. 113.

In *Weber* v. *City of Detroit*, 158 Mich. 149, 150, 122 N. W. 570, it is held that a statute imposing personal liability for special improvement assessments made prior to its enactment, where no such liability existed prior to its enactment, was void. For like reason a tax levied on property or an item of income for a period when it was exempt from taxation would be void.

The only adjudicated case bearing directly upon the precise point under discussion that I have been able to discover is the *Covington* case, *supra*. I find two other cases, however, that bear upon it indirectly and to my mind quite persuasively. *In the Matter of Pell*, 171 N. Y. 48, a statute was involved enacted in 1899 that imposed an inheritance tax upon all estates upon remainder or reversion which vested prior to the date of a previously enacted general inheritance tax statute but which would not come into actual possession or enjoyment until after the date of the enactment, to be taxed when the recipient came into possession. The statute was declared unconstitutional because its effect would be to "diminish the value of vested estates, to impair the obligation of a contract and take private property for public use without compensation" (p. 55). In the instant case the respondent's property in the $12,000 of income involved, became vested in him at the time he received it. Now to impose a tax upon it under the statute is to diminish its value, and to take property for public use without compensation precisely as much as did the New York statute stated.

In *Portunedo's Estate*, 20 Pa. Co. Ct. Rep. 419, an inheritance tax statute was involved that provided that "so much of estates of persons heretofore deceased as has not been actually distributed and paid to persons entitled thereto prior to the passage of this act shall be liable to the tax imposed by this law as well as the estates of persons who die hereafter." This was held unconstitutional on the ground that "when the right vested under existing laws is taxed by a subsequent law, for general purposes of government and not for any purpose specially benefiting the owner of such right, it is not only taking the property of such owner without compensation, but it is violating the other constitutional provision that taxes shall be equal." (p. 423). The

opinion quotes from 1 Kent 455: "A retrospective statute, affecting and changing vested rights is very generally considered in this country as founded on unconstitutional principles, and consequently inoperative and void."

It is stated in the opinion of the court that it has been held by this court and by the Supreme Court of the United States that income taxes are not void as retroactive if applied to recent transactions. The cases so holding were considering net income, as distinguished from individual items, and income received over a consecutive period next antecedent to the enactment of the taxing statute, not a period wholly disconnected with the time of the enactment and separated therefrom by an intervening period not subject to the tax imposed. It seems to me that the opinion of the court in effect concedes the invalidity of the retroactive feature of the tax when it says: "While the present tax may approach or reach the limit of permissible retroactivity it does not exceed it." It is not for the court to fix the limit of retroactivity. If income from dividends received in 1933 were properly subject to taxation why not those of 1932 or 1931? Why not go back to 1929, when dividends were many and large, instead of 1933, when they were few and small? The basis (1) of the court's rule by which to test the validity of the tax, that the year must be "sufficiently recent that the income of that year may reasonably be supposed to have some bearing on the present ability of the taxpayer to pay the tax," seems to be here absent. I see no connection between receipt of income from dividends in 1933 and present ability to pay a tax upon that item of income. Dividends of 1933 have "gone with the wind" by this time in all but comparatively few cases.

If it be conceded that because the dividends covered by the statute were not taxed as income during the year 1933 they might properly be subsequently taxed as *income* received during that year, the tax so imposed would have to be an income tax, computed at the income tax rate in force during that year, or the equal protection clause of the XIVth Amendment to the United States Constitution would be violated.

Dividends from Wisconsin corporations, which are the only ones within the statute, certainly cannot be taxed at a

higher rate than dividends from other corporations, else there is inequality. It is true that equality of rate within the class is the only equality necessary to validity of an income tax. But the mere fact that one corporation is a corporation organized under the laws of Wisconsin and another is a corporation organized under the laws of another state, cannot form a basis for taxing a recipient of a dividend fr the former and not taxing the recipient of a like dividend from the latter. Recipients of income constitute the class taxed under an income tax statute. If conceivably recipients of corporate dividends may constitute a separate class for income tax purposes, still all recipients of corporate dividends must constitute the class, not recipients of Wisconsin dividends only.

Under the instant section income from dividends is taxed at a rate entirely different from the rate imposed on incomes in 1933. A rate of taxation by the statute lower than the normal might conceivably be supported, because the corporation paid a tax on the earnings comprising the dividends, but a higher rate cannot possibly be. The first $2,000 of income under the statute involved would carry a slightly less tax than the normal tax, but on all above that the tax is higher. On the dividends received by the instant taxpayer the excess under the statute over the normal rate of 1933 is over $200. Moreover, taxpayers under the normal income tax law were entitled to offset capital losses. Such offset is denied by the instant statute. The instant taxpayer had large capital losses then deductible under the normal income tax statutes.

Counsel for respondent seem to contend in their briefs that the uniformity clause of the state constitution does not apply to income taxation because graduated rates of taxation are expressly provided for. But we have here something more than graduated rates. One class of income is taxed by one table of graduated rates, without deductions for capital losses, while all other kinds of income were taxed in 1933 at lower graduated rates with deductions for such losses. True the uniformity clause when the constitution was adopted applied only to property taxation because that taxation was the only kind then covered by the clause. See Art. VIII, sec. 1, as contained in the statutes of 1858. But

when the section was subsequently amended by adding thereto, the declaration of uniformity carried through, and it applies to all other species of taxation subsequently provided for, except as especially excepted by the terms of the amendment. This point is sufficiently covered by *Nunnemacher* v. *State*, 129 Wis. 190, 220, 108 N. W. 627, where it is said: "uniformity of taxation or even equality of taxation as applied to excise taxes must necessarily mean taxation which is not discriminatory but which operates alike on all persons similarly situated." There is the broad statement in *Appeal of Van Dyke*, 217 Wis. 528, 259 N. W. 700, that the uniformity clause does not apply to income taxes, but that is forthwith qualified by the statement that "the only uniformity required is uniformity within the class," and this implies a proper classification.

The inequalities above stated made the tax imposed upon the respondent void if it be considered as an income tax. The tax is referred to in the opinion of the court as a "special income tax." But it is not in my opinion an income tax at all but a property tax, and considered as such it is plainly violative of the uniformity clause of the state constitution. An income tax is a tax on income as a whole, not on individual items of income. It is a tax on net income, as distinguished from gross, and in computing it all items of income must be included. It has been said by this court several times that "In arriving at this amount (of the tax) the legislature takes the gross income of the taxpayer." *Fitch* v. *Wisconsin Tax Comm.*, 201 Wis. 383, 230 N. W. 37; *Wisconsin Ornamental I. & B. Co.* v. *Wisconsin Tax Comm.*, 202 Wis. 355, 229 N. W. 646. By "gross" income is there meant "total net" income as distinguished from gross receipts. The statement above quoted is made in relation to the normal income tax, but it necessarily applies to any tax that is an income tax as distinguished from other forms of tax. This court has also many times stated that the word "income" used in the constitutional amendment including income as a subject of taxation must be taken in its ordinary sense, and in its ordinary sense income means net income. It covers gains or profits and these cannot be ascertained from any single item of income. Income is defined in refer-

esce to income taxation as "the *amount* of wealth which comes to a person within a given period of time." 26 Ruling Case Law 147. "In constitutional and statutory provisions in regard to taxation . . . income appears to be uniformly construed as meaning net income, as opposed to gross receipts," Id. 149. With like reason it must be so construed as opposed to mere items of income. "Income means the balance of gain over loss," Id. 150. "The income tax is a general tax on all income." *Hudson* v. *U. S.*, 12 Fed. Suppl. 620. The "amount of wealth" acquired during a given period is not measured by a single item of income; "balance of gain over loss" cannot be based on a single item of income; a tax on a single item of income is not "a general tax on all income." The tax involved is a tax on a specified item of money received during the year, and as much a property tax as a tax on any other item of personalty received during the year would be, and if taxed at all would have to be taxed under the uniformity clause as other items of taxable personalty are taxed, unless there be a valid ground of distinction between money received as income and other items of personalty. Income from dividends might perhaps be so distinguished from some other items of income as to justify taxing the former and not the others, but I can conceive of no possible basis of classification as between dividends and interest. Whatever of distinction may be made between these two items would require dividends to be exempted rather than interest, for the source of the dividend—corporate earnings—has already been once taxed against the corporation, while the source of interest—the debt on which it is paid—has not been taxed at all. Whatever its nature may be considered to be the tax assessed against the respondent was in my opinion void under the uniformity clause of the state constitution and the equality clause of the XIV. th Amendment of the constitution of the United States and the judgment of the circuit court should be affirmed.

I am authorized to state that Mr. Justice Nelson concurs in this opinion.

EXHIBIT "D".

IN SUPREME COURT STATE OF WISCONSIN

AUGUST TERM, 1936.

No. 23.

EARLE S. WELCH, *Respondent*,

v.

ROBERT K. HENRY, State Treasurer, *Appellant*.

FAIRCHILD, *J.* (dissenting):

I cannot agree with the majority. It seems to me that the limits of the powers conferred upon the legislature by the people have been exceeded in this particular. It has never been considered fair play to impose burdens or penalties by later legislation upon a fellow citizen for an act or transaction which was lawful at the time of its occurrence, and the power to do that was withheld from governmental agencies by the people. The idea is not a new one and was not at the time of the formation of this government. Due process and the law of the land as legal concepts calculated to protect individuals in their lives and property have been parts of charters of freedom at least since the time of Conrad II (the Salic), who reigned from 1024 to 1039. In Mott's work on Due Process of Law, p. 1, he says with reference to an edict of that reign providing that no man be deprived of his fief, but by the laws of the empire and the judgment of his peers,

> "sixteen states of the United States have incorporated a literal translation of a portion of this canon into the fundamental law and fully as many more use phrases of similar import."

The thirty-ninth section of the Magna Carta reads, *Ibid*, p. 3,

> "No freeman shall be taken and imprisoned or disseized or exiled or in any way destroyed, nor will we go upon him nor send upon him, except by the lawful judgment of his peers and by the law of the land."

Sec. 6, ch. 15, Laws of 1935, is retroactive. I think it must be conceded that the taxpayer in this case had fully discharged all claims against him and his income under the law of 1933. Since this is so, his income for that year had been earned, taxed, and discharged of all obligations as income, and, under the "pattern of the income tax law", had passed from its status as income into the taxpayer's estate. Its character as income had vanished and whatever was left of it was no longer income, but was property and a part of the taxpayer's holdings or his estate. It has been decided that the legislature may constitutionally authorize the tax commission to go back several years for the purpose of reassessing incomes and correcting errors and eliminating frauds in previous returns. *State ex rel. Globe Steel Tubes Co.* v. *Lyons*, 183 Wis. 107, 197 N. W. 578. A legislature would not, of course, be acting under such constitutional power in levying a tax upon income not previously taxed at all. The power is merely that of collecting sums due since the tax was originally levied. It was held in *State ex rel. Globe Steel Tubes Co.* v. *Lyons, supra*, that this power included power retroactively to require payment of interest on back taxes from the date when they became due.

The legislature has also been upheld in levying new taxes on income already, but recently, earned. If this power to go back in levying new taxes is unlimited as to time, the tax in question would be valid. Can the legislature on March 14, 1935 levy a new tax upon incomes received during the calendar year 1933, or corresponding fiscal year? On July 13, 1911 the legislature imposed a tax on incomes received during the calendar year 1911. This act was upheld in *The Income Tax Cases*, 148 Wis. 456 at 514, 134 N. W. 673, 135 N. W. 164. On August 17, 1927, a tax was imposed upon incomes received in the calendar year 1926, and it was held valid in *West* v. *Tax Comm.*, 207 Wis. 557, 242 N. W. 165. In this case the tax on incomes received during 1926 as imposed by the law passed in 1925 was in the midst of the process of assessment when the 1927 law was passed.

Cooper v. *United States*, 280 U. S. 409, lays down the test that gains from "prior but recent transactions" may be

taxed as income. No case holds, and, with one exception, no case suggests, that the legislature may constitutionally impose a tax upon income received during a year, the taxes for which have been assessed and paid. *Stockdale* v. *The Insurance Companies*, 87 U. S. 323, holds good a tax imposed by Congress on July 14, 1870, on incomes received during the period from January 1, 1870 to August 1, 1870, but at page 331, the court says:

> "The right of Congress to have imposed this tax by a new statute, although the measure of it was governed by the income of the past year, cannot be doubted; much less can it be doubted that it could impose such a tax on the income of the current year, though part of that year had elapsed when the statute was passed. The joint resolution of July 4th, 1864, imposed a tax of five per cent. upon all income of the previous year, although one tax on it had already been paid, and no one doubted the validity of the tax or attempted to resist it."

Apart from the quoted remark in the *Stockdale* case, there is no authority for holding that after an income tax on income received during a given year has been assessed and collected, the legislature may constitutionally tax the income received that year to a further extent. Fairness suggests that when a taxpayer's tax on one year's income has been assessed and paid according to the law then in force, the taxpayer is justified in concluding that the matter is closed except for fraud or erroneous assessment. The power of the legislature to provide for the collection of taxes which validly should have been assessed under the existing law, but which were omitted because of fraud or mistake, cannot be doubted, but that power does not support the law here in question. There is no claim of fraud as a reason for reexamining and reassessing this income of 1933, but the legislature in 1935 seeks to reach into a citizen's present estate and lay a tax, called an income tax, on that portion of his present property which was income during 1933, but not thereafter, and by such so-called income tax, compel him to disgorge a sum of money into the com-

mon treasury. That he may be able to afford it is no more a sufficient excuse for the usurpation of power than is the great need by the treasury of money. Even though the need be great, constitutional rights should not be invaded. A desire for material to patch a leak does not warrant tearing away structure that prevents inundation.

> "When the government through its established agencies interferes with the title to one's property, or with his independent enjoyment of it, and its action is called in question as not in accordance with the law of the land, we are to test its validity by those principles of civil liberty and constitutional protection which have become established in our system of laws, and not generally by rules that pertain to forms of procedure merely." Cooley, Constitutional Limitations, (7th ed.) p. 505.

Civilized countries, enlightened nations have protected and preserved the rights of its citizens, encouraged thrift and the honest accumulation of resources. Laws relating to acts and events to occur in the future are acceptable and may be justified in taxation under the fundamental policy of protecting the rights of all and preserving the integrity of the government, but impositions on closed transactions cannot long be tolerated in a free government. Mr. Justice Story in the case of *The Society for Propagating the Gospel v. Wheeler*, 2 Gall. 139, defined a retroactive or, as he called it, a retrospective law:

> "Upon principle, every statute which takes away or impairs vested rights acquired under existing laws or creates a new obligation, imposes a new duty, or attaches a new disability, in respect to transactions or considerations already passed must be deemed retrospective."

I have adverted to the fact that the taxpayer's 1933 income discharged itself of impositions then existing. The majority opinion suggests many subtle differentiations, but these do not appear to me to build a substantial difference between the closed act which is beyond the reach of the legis-

lature and that particular situation of which the taxpayer complains.

I do not feel any practical purpose can be served by further discussion of the point. The feeling that persons who have income from dividends from Wisconsin corporations have escaped taxation long enough may exist, but such escape was purposely permitted by the legislature in the belief that a sufficient tax on that earning had been paid by the corporation. Income from such dividends might be taxed from 1935 on, but for the years that had closed, the legislature was precluded by its own determination that such income was sufficiently taxed at its source. Citizens acted in reliance upon the assurance of the government that if each did all the existing law required him to do, he need not worry about completed acts.

The objections to the act here outlined, together with those advanced by Mr. Justice Fowler in the dissent by him and Mr. Justice Nelson, sufficiently disclose the reasons for my not concurring in the majority opinion.

EXHIBIT "E".

IN SUPREME COURT, STATE OF WISCONSIN.

JANUARY TERM, 1938.

No. 72.

EARLE S. WELCH, *Appellant*,

vs.

ROBERT K. HENRY AND SOLOMON LEVITAN, as State Treasurer of the State of Wisconsin, *Respondents*.

Appeal from a judgment of the circuit court for Eau Claire County: James Wickham, Circuit Judge. *Affirmed.*

This action was begun by Earle S. Welch, Plaintiff, against Robert K. Henry and Solomon Levitan as Treasurer of the State of Wisconsin, defendants, to recover certain taxes paid by the plaintiff under protest. There was

a demurrer to the complaint. The demurrer was sustained. The plaintiff did not amend and judgment was entered on October 27, 1937, dismissing the plaintiff's complaint, from which judgment the plaintiff appeals.

Per CURIAM.

This case was before this Court and reported in *Welch* v. *Henry* (1937), 223 Wis. 319, 271 N. W. 68, to which reference is made for a statement of facts. On the former appeal and upon this appeal the plaintiff contends that the statute in question offends Sec. 1 of the fourteenth amendment to the constitution of the United Sates. Upon the former appeal this Court considered and rejected the plaintiff's contention that the act in question violated his rights under sec. 1 of the fourteenth amendment to the constitution of the United States. We have reconsidered plaintiff's contention and find nothing in the act violative of the plaintiff's rights under said section 1 of the fourteenth amendment. Reference is made to the opinion in that case and for the reasons there stated the judgment appealed from is affirmed.

Judgment affirmed.